



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

NO PROTEST RECEIVED
Release to Manager, ID Determinations - Cincinnati

DATE: [REDACTED]

SURNAME: [REDACTED]

Date:

JUL 15 2002

Contact Person: [REDACTED]

Identification Number: [REDACTED]

Contact Number: [REDACTED]

Employer Identification Number: [REDACTED]

Dear Applicant:

We have considered your application for recognition of exemption from federal income tax under section 501(a) of the Internal Revenue Code as an organization described in section 501(c)(3). Based on the information submitted, we have concluded that you do not qualify for exemption under that section. The basis for our conclusion is set forth below.

You were incorporated in the state of [REDACTED] on [REDACTED]. You filed your Application for Recognition of Exemption on [REDACTED]. Along with your Certificate of Incorporation, you submitted your By-Laws. [REDACTED] is your incorporator and registered agent.

Your By-Laws provide for the following offices: Executive Director, President, Secretary, and Treasurer, and such other positions that may be prescribed by the Board. Those holding the positions of Executive Director and president must be Board members. [REDACTED] serves as Executive Director. Your officers and directors, as listed in your [REDACTED] Form [REDACTED], consist of [REDACTED] and [REDACTED].

On [REDACTED], the [REDACTED] ([REDACTED]), a for-profit organization, was liquidated and its assets were gifted to you. Your application states that [REDACTED]'s function was to promote health and well-being. [REDACTED] and [REDACTED] owned 77% and 23%, respectively, of the business. [REDACTED] had rented a commercial site, where it sold health-related products, from [REDACTED] and his wife. In addition, [REDACTED] rented several of the offices in its leased space to individuals involved in health related services. Among the assets donated by [REDACTED] were furnishings and supplies for several offices, a dispensary inventory, gift certificates, a mailing list of clients, contract rights with health care practitioners who rented office space from [REDACTED], and an equipment lease. No new operating policies were initiated as a result of the transfer of assets from [REDACTED] to you.

[REDACTED]

Your Certificate of Incorporation states that the purposes for which you are organized are:

"To promote physical, mental and spiritual health and well-being by itself sponsoring, promoting or providing or by facilitating others to sponsor, promote or provide information, instruction, education, aid, products, services, research, empowerment and otherwise give help to people of the public at large with respect to healing, symptom relief, wellness maintenance and personal and spiritual development by drawing on the wide spectrum of complementary health care, Western and Eastern modalities, techniques, philosophies and thought."

You state that you plan to operate a market place open to the public that will provide a broad spectrum of health care information, services, and products by:

1. for a fee, providing office and classroom space; telephone and office reception; client scheduling; cashier services; public displays of print, video and poster information; and; publicity both on and off site to health practitioners;
2. selling remedies, health supplements and other health care related merchandise such as books, CD's, and personal care products. Items are sold at a 55% markup;
3. presenting and facilitating lectures, referral services, fairs and samplers both on and off site for which you will ask donations; and,
4. publishing a free health care-wellness focused magazine.

You further state that your future activities will include:

1. a health care education program for self care as well as certification to serve the public for which there will be a \$ application fee and for which you will receive 40% of attendance revenue;
2. a research program regarding clarification and innovation of health care products and/or services; and,
3. a funding program to help indigents pay for services available at the market place.

In a letter dated [REDACTED], you state that your educational services will include an annual [REDACTED] for which a nominal fee will be charged. Workshops conducted by lessees and other practitioners will be held (presenters pay a \$ application fee and 40% of their attendance revenue) and you plan to have a speaker program. In addition, you state that a program to assist indigents would be instituted so that (1) A sliding scale would be used where each practitioner would provide services at up to a 50% discount to 6-12 clients per year; and (2) up to 100% of the practitioners' fees would be paid for some individuals using funds which you hope to receive from outside sources. You also state that you publish an educational website—a downloaded copy is attached.

On [REDACTED], you leased from [REDACTED] commercial space that had been leased to [REDACTED]. You then subleased ten offices at the location to twenty tenants who provided services, workshops, and classes in areas such as acupuncture, chiropractic, aromatherapy, podiatry, gynecology, herbology, tai chi instruction, yoga instruction, music for healing, meditation, internal medicine, past life regression, and prenatal massage. With the exception of [REDACTED], your Board members and officers are tenants in the building.

in a letter dated [REDACTED] you state that there was a lot of turnover in the practitioners because many "were unable to make a go of it."

A "Rider to Lease" includes twenty-two additional conditions for leasing office space. Among the additional terms contained in the rider:

1. Tenants may not sell their services or products on the premises without your approval.
2. Tenants are required to pay you 7½% of their gross income from any services and products that they sell on the premises. You describe such income as "staff fees" rather than rent.
3. All clients are to be scheduled through your administrative office.
4. Payments for services and products provided by the tenants are to be made through your administrative office. The clients' payments are to be made in your name and held in a trust account by you. You have the sole discretion in determining whether any of the fees are to be used towards amounts that may be owed to you before the collected amounts are released to the tenant.
5. During the term of the lease and for one year after the lease's termination or expiration, tenants are forbidden from taking clients (obtained or treated on the premises) to another location or office.
6. At your request, tenants are required to present without charge information, demonstrations, presentations, seminars and lectures in their specialty. You have the right to record and/or videotape the presentations for your own use and ownership.
7. At your request, tenants are required to prepare descriptive literature and participate in video preparations. Any printed and recorded material becomes your property.
8. Tenants are to be considered independent contractors.

You publish a free health care magazine for which you receive revenue from the sale of advertisement space to health care related businesses. Individuals who are presenters or tenants at your center provide the articles. Individual donations are solicited in the magazine.

The following information is based upon projected figures that you provided regarding your second and third years of operation.

Income Sources Expressed as Percent of Total Support to Be Received

<u>Income Source</u>	<u>Year 2</u>	<u>Year 3</u>
Fees charged to health care practitioners	67%	67%
Health Care Product Sales	17.9%	18%
Annual Health Festival	4.4%	4.3%
Workshop fees	1.3%	1.2%
Gifts/Grants/ Contributions	0.69%	0.76%

Expenses Expressed as Percent of Total Amount

<u>Expenses</u>	<u>Year 2</u>	<u>Year 3</u>
Rent	45.0%	43.8%
Salaries for receptionists/office manager	23.6%	24.5%
Magazine Related Expenses	13.1%	12.9%
Health Care Product Inventory	11.5%	12.1%
Annual Health Festival	0.21%	0.2%
Gifts/Grants/Contributions	0.0%	0.0%

Section 501(c)(3) of the Code provides, in part, for the exemption from federal income tax of organizations organized and operated exclusively for educational purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Section 513(a) of the Code defines the term "unrelated trade or business" as any trade or business the conduct of which is not substantially related (aside from the need of such organization for income or funds or the use it makes of the profits derived) to the exercise or performance by such organization of its charitable, educational, or other purpose or function forming the basis for its exemption under section 501.

Section 513(c) of the Code provides that with respect to advertising and similar activities, the term "trade or business" includes any activity which is carried on for the production of income from the sale of goods or the performance of services. An activity does not lose identity as a trade or business merely because it is carried on within a larger aggregate of similar activities or within a larger complex of other endeavors which may, or may not, be related to the organization's exempt purposes.

Section 1.501(c)(3)-1(c)(1) of the Income Tax Regulations provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3) of the Code. An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(d)(2) of the Income Tax Treasury Regulations provides that the term "charitable" is used in Section 501(c)(3) of the Income Tax Code in its general accepted legal sense.

Section 1.501(c)(3)-1(d)(3) of the Income Tax Regulations defines the term "educational" as the instruction of the public on subjects useful to the individual and beneficial to the community.

Section 1.501(c)(3)-1(e)(1) of the Income Tax Regulations provides that an organization may meet the requirements of section 501(c)(3) although it operates a trade or business as a substantial part of its activities, if the operation of such trade or business is in furtherance of the

organization's exempt purpose or purposes and if the organization is not organized or operated for the primary purpose of carrying on an unrelated trade or business, as defined in section 513.

Section 1.513-1(d)(2) of the Income Tax Regulations provides that a trade or business is related to exempt purposes only where the conduct of the business activities has causal relationship to the achievement of exempt purposes (other than through the production of income) and it is substantially related only if the causal relationship is a substantial one. It further provides that the production or distribution of the goods or the performance of the services from which the gross income is derived must contribute importantly to the accomplishment of the exempt purposes.

Section 1.513-1(d)(4)(iv) of the Income Tax Regulations, in Example 7, describes advertising activity in an exempt organization's journal. Although continuing education of its members in matters pertaining to their profession was one of the purposes for which the organization was granted exemption, the publication of advertising was found not to be an educational activity and the income which the organization derived from advertising constituted gross income from unrelated trade or business.

In United States v. Wells Fargo Bank, 485 U.S. 351, 108 S. Ct. 1199 (1990) the Court held that an organization must prove unambiguously that it qualifies for tax exemption.

In Harding Hospital, Inc. v. United States, 505 F.2d 1068 (6th Cir. 1974), the court held that an organization seeking a ruling as to recognition of its tax exempt status had the burden of proving that it satisfies the requirements of the particular exemption statute. Whether an organization has satisfied the operational test is a question of fact. See also, Christian Stewardship Assistance, Inc. v. Commissioner, 69 T.C. 1037, 1042 (1978).

In Better Business Bureau v. United States, 316 U.S. 279 (1945), the Court held that the existence of a single non-exempt purpose, if substantial in nature, will destroy a charitable exemption.

In American Institute for Economic Research v. United States, 302 F.2d 934 (1962), cert. denied, 372 U.S. 976 (1963), the Court held that a determination must be made regarding whether the business activities of an organization are incidental to its charitable objectives or whether the converse is true in evaluating an entity engaged in commercial activity. The Court found that competition with commercial firms constitutes strong evidence of a substantial nonexempt purpose.

In Living Faith Inc. v. Commissioner, 950 F.2d 365 (7th Cir. 1991), the court held that the purposes of an organization may be inferred from the activities in which it engages. Among the factors considered by the Court were the commercial hue or nature of the activities, the competitive nature of the activities, the existence of accumulated profits, and the provision of free or below cost services.

In B.S.W. Group, Inc. v. Commissioner, 70 T.C. 352, the Court found that where an exempt organization provided consulting services to tax-exempt and not for profit clients, a negative factor in determining whether the activity was in furtherance of an exempt purpose was

the organization's failure to limit its clientele to organizations which are themselves section 501(c)(3) exempt organizations

In Federation Pharmacy Services, Inc., 72 T.C. 687 (1979), aff'd., 625 F.2d 804 (8th Cir. 1980), the Court held that an organization operated a pharmacy primarily for commercial purposes where it sold drugs at a discount determined by its cost, with no provision for sales below cost to the elderly and handicapped. In its ruling, the court stated that the fact that the products sold aided health did not entitle an organization to an automatic exemption under section 501(c)(3) of the Code. The sale of such products, without more, is not in furtherance of a charitable purpose.

In Hillcrest Country Club, Inc. v. U.S., 152 F.Supp. 896 (DC Mo. 1957), the Court held that where a corporation is organized to take over the activities of a predecessor, the court may consider the predecessor's activities in determining the purposes for which a corporation is organized.

In Lorain Avenue Clinic v. Commissioner, 31 T.C. 141 (1958), the Court held that a nonprofit corporation chartered as a clinic for doctors and dentists, which charged moderate fees or gave free service to a small percent of persons, was not operated exclusively for charitable purposes.

Rev. Rul. 69-545, 1969-2 C.B. 117, states "(I)n the general law of charity, the promotion of health is considered to be a charitable purpose." The ruling goes on to say that more is required to be tax-exempt under Section 501(c)(3) of the Code.

Rev. Rul. 69-572, 1969-2 C.B. 119, held that where an exempt organization that had a close relationship in its purposes and functions with other exempt organizations leased space to the organizations at substantially below fair rental value in a non-commercial manner, the arrangement was in furtherance of charitable purposes. Although the rental activity was not inherently charitable, the activity enabled the exempt organizations to further their charitable purposes.

Rev. Rul. 72-369, 1979-C.B. 245, held that a nonprofit organization formed to provide managerial and consulting services at cost to unrelated 501(c)(3) organizations to improve the administration of their charitable programs did not qualify for exemption under section 501(c)(3) of the Code. The organization entered into agreements with unrelated nonprofit organizations to furnish managerial and consulting services on a cost basis. The Service reasoned that providing managerial and consulting services on a regular basis for a fee is trade or business ordinarily carried on for profit. The fact that the services were provided at cost and solely for exempt organizations was not sufficient to characterize this activity as charitable under section 501(c)(3). Furnishing the services at cost lacked the donative element necessary to establish this activity as charitable. This case was distinguished from Rev. Rul. 71-529, 1971-2 C.B. 234, where an organization controlled by a group of exempt organizations provided investment management services for a charge substantially less than cost (less than 15% of cost) solely to that group.

If an organization operates a trade or business as a substantial part of its activities, in

order to be tax-exempt, the organization that must show that it was not organized or operated primarily to carry on the unrelated trade or business and it must show that the operation of such trade or business furthers its exempt purpose or purposes. Section 1.501(c)(3)-1(e)(1) of the Income Tax Regulations. Under Section 1.501(c)(3)-1(c)(1), an organization is not considered to be operated exclusively for one or more exempt purposes if more than an insubstantial part of its activities is not in furtherance of an exempt purpose. A single, substantial non-exempt purpose will preclude a charitable exemption. Better Business Bureau v. United States, supra.

In providing services or goods, an exempt organization must not do so merely as a means for producing income: the activity must contribute importantly to the organization's carrying out of its exempt purposes. Section 1.513-1(d)(2) of the Income Tax Regulations. In Living Faith, Inc. v. Commissioner, supra, the court set forth factors to be considered when determining what an organization's purposes are.

You state that your purpose is to educate the public and to promote health awareness and that your proposed activities are all in furtherance of this purpose. In Federation Pharmacy Stores, supra, the court noted that "(v)irtually everything we buy has an effect, directly or indirectly, on our health. We do not believe that the law requires that any organization whose purpose is to benefit health, however remotely, is automatically entitled, without more, to the desired exemption...While the promotion of health is recognized as being charitable in nature, more is needed in order to establish that you qualify for recognition as an exempt organization." See also, Rev. Rul. 69-545, supra.

Your rental of space to businesses that provide services in areas related to holistic health concerns is not in itself an activity in furtherance of a charitable purpose. Commercial enterprises are also engaged in the rental of space to such businesses as evidenced by your for-profit predecessor's involvement in such leases.

Your tenants consist of businesses, not tax-exempt under section 501(c)(3), that charge for their services and products. You have made it a condition of the lease that you be paid a portion of the gross profits from the tenants' gross revenue from such sales. You have set up a system whereby you receive payments for the services and products directly, and after determining whether you are owed any fees, you disburse the remainder to the lessors. You state that many of the tenants have experienced financial difficulties and as a result, have left your building.

Even though these activities, which are operated on a part-time basis at your location, may not generate a profit for some, they are being conducted as a trade or business, not as a charitable endeavor on the part of the lessors. The fact that you require the tenants to provide discounted services to between 6-12 clients per year does not render their activity charitable. See, e.g., Lorain Avenue Clinic v. Commissioner, supra. Commercial operations often offer discounted services as an enticement to attract customers. Your rental of space to entities that are not tax-exempt does not serve to further your stated charitable purposes nor any charitable purposes by organizations recognized as exempt under section 501(c)(3). See, B.S.W. Group, Inc. v. Commissioner, supra, and Rev. Rul. 69-572, supra.

[REDACTED]

In assessing whether there were charitable purposes being furthered in the sale of discounted drugs to the elderly and disabled, the court in Federation Pharmacy Stores, supra, stated that "we fail to see how the fact that (an organization) happens to deal in drugs can convert it to a section 501(c)(3) organization. If it could be so converted, then so could a store selling orthopedic shoes, crutches, health foods, or any other product beneficial to health". In that case, the fact that the drugs were offered at a discount was insufficient to prove that the activity furthered a charitable purpose since commercially operated pharmacies often discounted products. Your sale of such products would put you in direct competition with for-profit companies engaged in the same type of business. And, your proposal to sell the products at a 55% markup leaves no doubt as to the profit making aspects of the activity... See also, American Institute for Economic Research v. United States, supra.

Your activities related to the rental of space to health care related individuals and the sale of health care products, activities in which your predecessor also engaged, do not serve to further your charitable purposes. The "commercial hue" referred to in Living Faith Inc. v. Commissioner, supra, is clearly present in these activities. Even assuming that the activities are structured so as to produce revenue to fund any charitable activities, this does not alter the fact that they are not charitable endeavors. Section 1.513-1(d)(2) of the Income Tax Regulations; Rev. Rul. 72-369.

While you offer a free newsletter and you conduct some educational workshops and seminars, these activities appear to be incidental to your functioning. Even your newsletter appears designed largely to generate business for the authors of the articles. The amounts that you receive and pay out as gifts, grants and contributions, as well as the discounted services that are provided to some individuals through the lease terms imposed on the tenants, are minimal. Most your support is derived from the rental of office space, health products sales, and revenue from the newsletter you print, and the majority of your expenses and activities are related to commercial activities. Considering the overall operation of your organization, it is evident that any charitable activities in which you plan to be engaged would be so minor as not to qualify you for an exemption. Better Business Bureau v. United States, supra.

You have failed to meet your burden under Harding Hospital, Inc. v. United States, supra, to demonstrate that you have been organized and operated exclusively for exempt purposes by serving a public rather than a private interest.

Accordingly, you do not qualify for exemption as an organization described in section 501(c)(3) of the Code and you must file federal income tax returns.

Contributions to you are not deductible under section 170 of the Code.

You have the right to protest this ruling if you believe it is incorrect. To protest, you should submit a statement of your views to this office, with a full explanation of your reasoning. This statement, signed by one of your officers, must be submitted within 30 days from the date of this letter. You also have a right to a conference in this office after your statement is submitted. You must request the conference, if you want one, when you file your protest statement. If you are to be represented by someone who is not one of your officers, that person will need to file a

[REDACTED]

proper power of attorney and otherwise qualify under our Conference and Practices Requirements.

If you do not protest this ruling in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the Code provides, in part, that a declaratory judgement or decree under this section shall not be issued in any proceeding unless the Tax Court, the United States Court of Federal Claims, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted administrative remedies available to it within the Internal Revenue Service.

If we do not hear from you within 30 days, this ruling will become final and a copy will be forwarded to the Ohio Tax Exempt and Government Entities (TE/GE) office. Thereafter, any questions about your federal income tax status should be directed to that office, either by calling 877-829-5500 (a toll free number) or sending correspondence to: Internal Revenue Service, TE/GE Customer Service, P.O. Box 2508, Cincinnati, OH 45201. The appropriate State Officials will be notified of this action in accordance with Code section 6104(c).

When sending additional letters to us with respect to this case, you will expedite their receipt by using the following address:

Internal Revenue Service
[REDACTED] T:EO:RA:T:2
1111 Constitution Ave. N.W.
Washington, D.C. 20224

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

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Joseph Chasin
Acting Manager, Exempt Organizations
Technical Group 2

Enclosure:
Website [REDACTED]

[REDACTED] [REDACTED]